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Memorandum for: Ernie Chase
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Attached are basic assumptions
we used in modeling a 25 percent reduction
in oil prices. [redacted]
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ASSUMPTIONS USED FOR OIL-PRICE CUT SIMULATIONS, FEBRUARY 1983

1. In establishing the OECD baseline case we assume the following rates of real GNP growth, inflation rates, and levels of current account surplus or deficit:

Real GNP Growth Rate

	<u>US</u>	<u>Germany</u>	<u>Japan</u>	<u>Canada</u>	<u>France</u>	<u>U.K.</u>	<u>Italy</u>	<u>Other OECD</u>	<u>All OECD</u>
1983	3.0	.0	2.7	1.3	.5	2.1	.2	.7	1.8
1984	3.0	2.4	4.2	2.0	2.5	2.8	3.0	3.0	3.0
1985	3.0	3.0	4.5	3.0	3.0	3.0	4.0	3.5	3.3

Inflation Rate

	<u>US</u>	<u>Germany</u>	<u>Japan</u>	<u>Canada</u>	<u>France</u>	<u>U.K.</u>	<u>Italy</u>	<u>Other OECD</u>	<u>All OECD</u>
1983	5.5	3.8	2.7	7.5	10.0	6.1	15.7	10.7	7.5
1984	6.0	4.0	3.4	7.0	8.9	8.0	15.0	14.8	8.9
1985	6.0	4.0	3.0	7.0	8.0	8.5	15.0	13.9	8.9

Current Account Balance

	<u>US</u>	<u>Germany</u>	<u>Japan</u>	<u>Canada</u>	<u>France</u>	<u>U.K.</u>	<u>Italy</u>	<u>Other OECD</u>	<u>All OECD</u>
1983	-31.2	5.6	12.0	.8	-9.1	4.8	-4.0	-22.4	-43.5
1984	-25.1	7.3	8.2	-.0	-6.4	2.1	-3.0	-20.0	-37.0
1985	-20.1	5.0	7.1	-.0	-6.0	1.0	-2.0	-20.0	-35.0

2. For each major country there are dozens of assumed values, some representing government policy variables, others representing values we do not choose to estimate econometrically. Among the more important of these variables are the following:

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Growth in Money Supply

	<u>US</u>	<u>Germany</u>	<u>Japan</u>	<u>Canada</u>	<u>France</u>	<u>U.K.</u>	<u>Italy</u>	<u>Other OECD</u>
1983	8.0	7.0	9.0	10.0	9.5	10.0	17.5	11.0
1984	8.0	7.0	9.0	8.0	10.0	9.0	16.5	11.0
1985	9.0	7.0	9.0	10.5	11.0	9.0	16.5	11.0

Discount Rate (or equivalent)

	<u>US</u>	<u>Germany</u>	<u>Japan</u>	<u>Canada</u>	<u>France</u>	<u>U.K.</u>	<u>Italy</u>	<u>Other OECD</u>
1983	8.0	7.0	6.5	11.0	9.5	9.0	18.0	8.0
1984	8.0	7.0	6.5	10.0	9.5	9.0	18.0	8.0
1985	7.5	7.0	6.5	10.0	9.5	9.0	18.0	7.5

Growth in Nominal Total Government Consumption

	<u>US</u>	<u>Germany</u>	<u>Japan</u>	<u>Canada</u>	<u>France</u>	<u>U.K.</u>	<u>Italy</u>	<u>Other OECD</u>
1983	6.8	-2.6	4.3	10.4	5.4	12.7	11.9	17.4
1984	5.9	2.2	5.4	8.9	13.6	12.2	16.2	23.9
1985	7.4	2.5	3.9	11.4	11.3	13.6	14.2	23.7

Note: Nominal Government spending figures shown are not based on projected budget data, rather they are model-derived figures which ensure consistency between the estimates, particularly the GNP growth estimates.

Exchange Rate Change (percent)

	<u>Germany</u>	<u>France</u>	<u>U.K.</u>	<u>Japan</u>	<u>Canada</u>	<u>Italy</u>
1983	+5.2	-3.0	-4.5	4.1	-4.5	-6.5
1984	+5.8	-2.0	-2.6	5.9	-3.6	-5.6
1985	+6.3	-0.6	-2.9	7.4	-1.8	-5.4

Note: In the baseline scenario exchange rates are assumed to adjust in proportion to the change in relative inflation rates in these countries and the US.

3. In the 25% oil-price cut scenario, we assume that the nominal money supply, nominal government spending, and the exchange rate changes shown above are all unchanged. We assume, however, that the discount rate changes enough so that real interest rates are unchanged from the baseline scenario.

1985 Distribution: 2.5 3.0 11.4 11.3 13.6 14.2 23.7
 Orig - LDX to Ernie Chase, Treasury
 4 - IMC/CB
 1 - EURA
 2 - EURA Production
 1 - EURA/EI
 2 - EURA/EI/EI
 1 - Author
 DDI/EURA/EI/EI [redacted] (8Mar.83)

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